IN THE HIGH COURT OF PUNJAB AND HARYANA AT CHANDIGARH

ITR No.570 of 1995
Date of decision:15.9.2006

Commissioner of Income Tax, Patiala

...Petitioner

v.

Punjab Tractors Limited Mohali.

...Respondent

CORAM: HON'BLE MR. JUSTICE ADARSH KUMAR GOEL
HON'BLE MR. JUSTICE AJAY KUMAR MITTAL

Present: Dr. N.L.Sharda, Advocate for the revenue.
Mr. PC Jain, Advocate with Ms.Rimpy Chaudhary, Advocate, for the respondent.

JUDGMENT:

Following questions of law have been referred for opinion of this Court by the Income Tax Appellate Tribunal, Chandigarh Bench, Chandigarh arising out of its order dated 23.12.1994, RA No.66/CHANDI/95, in respect of assessment year 1985-86:-

"i) Whether, on the facts and in the circumstances of the case, the Tribunal was right in law in excluding the expenditure on repairs of cars as well as expenditure incurred on running and maintenance of vehicles other than cars, while working out disallowance under section 37(3A) of the Income Tax Act?

ii) Whether, on the facts and in the circumstances of the case, the ITAT was right in law in upholding the order of the CIT(A) deleting addition of Rs.85000/- made by the AO in view of section 37(4) on account of rent paid by the assessee for Guest House, holding that the same was allowable as a valid deduction under section 30?

iii) Whether, on the facts and in the circumstances of the case, the ITAT was right in law in upholding the order of the first appellate authority regarding disallowance made by the AO under section 40A(5)?

iv) Whether, on the facts and in the circumstances of the case, the ITAT has erred in directing the AO to re-compute the capital employed and allow deduction under section 80J in respect of Foundry Unit, after excluding liability on pro rata basis?"

Facts noticed by the Tribunal are that the assessee-company had shown expenditure on the maintenance of cars and other vehicles. Disallowance was made at Rs.19,62,269/-. The assessee's plea was that the expenditure on repairs of cars must be excluded from the expenses on running and maintenance of cars because such expenditure was not covered under section 37(3A) of the Income Tax Act, 1961 (for short, 'the Act') It was pointed out that there was a specific provision relating to expenditure on repairs under sections 31 and therefore, section 37 of the Act which was a residuary section, would not come into play. Expenditure on repairs amounted to Rs.3,18,067/-. It was further explained that a sum of Rs.13,44,281/- represented expenditure on the maintenance of other vehicles like jeeps, buses, motor-cycles, tractors, etc. Disallowance under section 37(3A) related to 'motor-car' only and since 'other vehicles' were not covered by the said provision, disallowance of Rs.13,44,281/- under section 37(3A) was said to be not permissible in law. The Tribunal agreed with the plea and held that the expenditure on petrol and maintenance of motor-cars was only covered under section 37(3A) of the Act. Following the earlier order of the Tribunal relating to the preceding assessment year, expenditure on repairs was also excluded. Since other vehicles were not covered under section 37(3A) of the Act, expenditures on vehicles other than cars were also excluded from the disallowance made under section 37(3A) of the Act.

The assesse had paid rent amounting to Rs.85000/- to the Punjab State Industrial development Corporation. The assessing Officer took the view that payment of rent in respect of Guest House could not be

allowed as a deduction under section 37(4) of the Act. The first appellate authority, however, restored the issue to the file of the assessing officer for fresh consideration, after verification, following his earlier order relating to assessment year 1981-82. The assessee's plea was that deduction was to be allowed under section 30 of the Act. When the matter came before the Tribunal in the revenue's appeal, it was noticed that in the preceding assessment year, similar question had arisen and the assessee's plea was accepted. The same view was taken and deduction in respect of payment of rent was allowed.

The assessing officer noted that a sum of Rs.85000/- had been paid by the assessee company to the Vice chairman as salary and Rs.34,049/- by way of other allowances. The assessing officer allowed a sum of Rs.12000/- out of payments made at Rs.28,422/-. Balance amount of Rs.16,422/- was disallowed. Similarly, salary was paid at Rs.85000/- to the Managing Director and other allowances at Rs.28,148/-. Here also, the assessing officer allowed allowance at Rs.12000/- only. When the matter went in appeal, the first appellate authority deleted the disallowance, following his order relating to assessment year 1983-84. When the matter came before the Tribunal in the revenue's appeal, it was noticed that a similar question had arisen in the preceding assessment year and the assessee's plea was accepted, following an earlier order relating to assessment year 1981-82 and disallowance made under section 40A(5) of the Act was deleted.

The assessee had made claim under section 80J of the Act in respect of its foundry unit. The dispute had arisen about the computation of capital employed in the unit. The precise question which had arisen related to certain liabilities which were required to be excluded on proportionate basis. The first appellate authority directed the assessing officer to re-compute the capital employed in the unit, while allowing deduction under section 80J of the Act. When the matter came before the Tribunal in the revenue's appeal, it was noticed that in the preceding assessment year also, a similar question had been raised by the revenue but it was declined and the assessee's plea was accepted.

We have heard learned counsel for the parties. We proceed to decide the above questions as under:-

Question No.(i)

On this question, the Tribunal held that expenditure on repairs and on other vehicles was not disallowance under section 37(3A) of the Act, as disallowance under the said section covers only "motor cars".

Sub-section (3A) relevant to the assessment year 1985-86 was as under:-

> "(3A) Notwithstanding anything contained in sub-section (1), where the expenditure or, as the case may be, the aggregate expenditure incurred by an assessee on any one or more of the items specified in sub-section (3B) exceeds one hundred thousand rupees, twenty per cent of such excess shall not be allowed as deduction in computing the income chargeable under the head "Profits and gains of business or profession."

Learned counsel for the assessee has also referred to sub-section (3B), which is as under:-

> "(3B) The expenditure, referred to in sub-section (3A) is that incurred on -
> (i) advertisement, publicity and sales promotion; or
> (ii) running and maintenance of aircraft and motor cars; or
> (iii) payments made to hotels
> Explanation – For the purposes of sub-section (3A) and (3B) -
> (a) the expenditure specified in clause (i) to clause (iii) of sub-section (3B) shall be the aggregate amount of expenditure incurred by the assessee as reduced by so much of such expenditure as is not allowed under any other provisions of this Act;
> (b) expenditure on advertisement, publicity and sales promotion shall not include remuneration paid to employees of the assessee engaged in one or more of the said activities;

> (c) expenditure on running and maintenance of aircraft and motor cars shall include -
> (i) expenditure incurred on chartering any aircraft and expenditure on hire charges for engaging cars plied for hire;
> (ii) conveyance allowance paid to employees and, there the assessee is a company, conveyance allowance paid to its directors also."

Learned counsel for the assessee submitted that words "running and maintenance of motor cars" did not refer to "repairs" and also did not cover vehicles other than "motor cars".

We are unable to accept this submission to the extent of repairs though we accept the submission with regard to vehicles other than motor cars. The words "expenditure on running and maintenance of" cannot exclude the word "repairs". Considering the scheme of Section 37 of the Act, the Hon'ble Supreme Court in recent judgment in **Britannia Industries Limited v. Commissioner of Income tax and another,** (2005) 278 ITR 546 held in the context of Section 37(4) of the Act that benefits indicated in Sections 30 to 36 of the Act will not be available on the issues covered under section 37 of the Act. It was held that expenses towards rent, repairs will also be deemed to be covered by expression "maintenance". On the same analogy, we hold that expenses on "repairs" will be covered by the expression "running and maintenance" used in section 37(3B) of the Act. However, since disallowance is confined to "motor cars", the same will not apply to other vehicles.

We, thus, hold that expenditure on repairs of motor cars is not excluded for the purpose of disallowance under section 37(3A) of the Act but expenditure on other vehicles is excluded. The question is answered accordingly.

Question No.(ii)

This question is covered by judgment of the Hon'ble Supreme Court in **Britannia Industries Limited's** case (supra), wherein it was observed:-

> ".....In our view, the intention of the Legislature appears to be clear and unambiguous and was intended to exclude the expenses towards rents, repairs and also maintenance of premises/accommodation used for the purposes of a guest house of the nature indicated in sub-section(4) of section 37. When the language of a statute is clear and unambiguous, the courts are to interpret the same in its literal sense and not to give it a meaning which would cause violence to the provisions of the statute. If the Legislature had intended that deduction would be allowable in respect of all types of buildings/accommodations used for the purposes of business or profession, then it would not have felt the need to amend the provisions of section 37 so as to make a definite distinction with regard to buildings used as guest houses as defined in sub section (5) of section 37 and the provisions of sections 31 and 32 would have been sufficient for the said purpose. The decisions cited by Dr. Pal contemplate situations where specific provision had been made in sections 30 to 36 of the Act and it was felt that what had been specifically provided therein could not be excluded under section 37. The clarification introduced by way of sub-section (5) to section 37 was also not considered in the said case."

Learned counsel for the assessee referred to certain High Court judgments particularly, Full Bench judgment of the Kerala High Court in **CIT v. Travancore Cements Limited,** (1999) 240 ITR 816, taking the view that expenditure permissible under Sections 30 to 36 of the Act is not excluded under section 37(3A) of the Act but this view cannot be accepted in view of judgment of the Hon'ble Supreme Court in **Britannia Industries Limited's** case (supra).

In view of above judgment, order of CIT(A) and ITAT deleting addition on account of rent paid by the assessee for the guest house was

erroneous. The question is answered in favour of the revenue and against the assessee.

Question No.3

Relevant sub-section for the assessment year in question was as under:-

> "40A(5)(a) where the assessee -
> (i) incurs any expenditure which results directly or indirectly in the payment of any salary to an employee or a former employee, or
> (ii) incurs any expenditure which results directly or indirectly in the provision of any perquisite (whether convertible into money or not) to an employee or incurs directly or indirectly by expenditure or is entitled to any allowance in respect of any assets of the assessee used by an employee either wholly or partly for his own purposes or benefit,
>
> then, subject to the provisions of clause (b), so much of such expenditure or allowance as is in excess of the limit specified in respect thereof in clause (c) shall not be allowed as a deduction:
>
> Provided that where the assessee is a company, so much of the aggregate of -
> (a) the expenditure and allowance referred to in sub-clauses(i) and (ii) of this clause; and
> (b) the expenditure and allowance referred to in sub clauses(i) and (ii) of clause (c)of section 40,
> in respect of an employee or a former employee, being a director or a person who has a substantial interest in the company or a relative of the director or of such person, as is in excess of the sum of one hundred and two thousand rupees, shall in no case be allowed as a deduction:
>
> Explanation 2 – In this sub-section -
> (a) 'salary' has the meaning assigned to it in clause (1)

read with clause (3) of section 17 subject to the following modifications, namely:-

(1) in the said clause(1), the word 'perquisites' occurring in sub-clause (iv) and the whole of sub-clause (vii) shall be omitted;

(2) in the said clause (3), the references to 'assessee' shall be construed as references to 'employee or former employee' and the references to 'his employer or former employer' and 'an employer or a former employer' shall be construed as references to 'the assessee';

(b) 'Perquisite' means -

(i) rent-free accommodation provided to the employee by the assessee;

(ii) any concession in the matter of rent respecting any accommodation provided to the employee by the assessee;

(iii) any benefit or amenity granted or provided free of cost or at concessional rate to the employee by the assessee;

(iv) payment by the assessee of any sum in respect of any obligation which, but for such payment, would have been payable by the employee; and

(v) payment by the assessee of any sum, whether directly or indirectly or through a fund, other than a recognised provident fund or an approved superannuation fund, to effect an assurance on the life of the employee or to effect a contract for any annuity."

Learned counsel for the assessee submitted that this question is covered in favour of the revenue by judgment of the Hon'ble Supreme Court in **CIT v. Mafatlal Gangabhai and company (P) Limited,** (1996) 219 ITR 644, wherein it was held that disallowance under section 40A(5) the Act did not apply to payment made in cash. It was observed:-

"On a consideration of both the points of view, we are inclined to agree with the submission of learned counsel

> for the assessees. The language employed in the sub-clause is not capable of taking within its ambit cash payments made to the employees by the assessee. These cash payments will, of course, be treated as salary paid to the employees and will be subject to the limits/ceiling, if any, in that behalf. But they cannot be brought within the purview of the words "any expenditure which results directly or indirectly in the provision of any benefit or amenity or perquisite" - more so because of the following words - "whether convertible into money or not."

From the statement of case, we do not find that payment made by the assessee was a cash payment. Accordingly, answer to the question has to be in favour of the revenue and against the assessee.

Question No.iv:

Learned counsel for the assessee relied upon judgment of Bombay High Court in **Indian Oil Corporation Limited v. S.Rajagopalan Income tax Officer, Companies, Circle II(1) Bombay and others,** (1973) 92 ITR 241, wherein it was held that the assessee was entitled to certain liabilities on proportionate basis and have the capital employed re-computed accordingly under section 80J of the Act. Relevant observations in the said judgment are:-

> "Section 80J(1) provides that the assessee is to be allowed a deduction of 6% per annum on the capital employed in the industrial undertaking from the gross total income of the assessee. Rule 19A provides for computation of capital employed in an industrial undertaking. Sub-rule(1) provides that for the purpose of section 80J the capital employed in an industrial undertaking shall be computed in accordance with sub-rules(2) to (4). Sub-rule (2) provides that the aggregate of the amounts representing the values of the assets as on

the first day of the computation period of the undertaking shall first be ascertained. Sub-rule (3) provides that from the aggregate of the amount so ascertained under sub-rule (2) shall be deducted the aggregate of the amounts as on the first day of the computation period of borrowed moneys and debts due by the assessee. At first look sub-rules (2) and (3) appear to provide that from the aggregate value of the assets of each undertaking the aggregate of the liabilities of the assessee shall be deducted. The assessee in this case owns 4 industrial undertakings. The result of such interpretation would be that from the assets of each industrial undertaking the entire borrowings of the assessee in respect of all the industrial undertakings are to be deducted for arriving at the capital employed in an industrial undertaking. On the face of it, this is an absurd proposition. If you want to arrive at the capital employed by an assessee in a particular industrial undertaking, you cannot arrive at it by deducting from the assets of that particular undertaking the liabilities not only of that industrial undertaking but also of three other industrial undertakings. This is mathematically absurd. What you want to find is the capital employed in an industrial undertaking. This cannot be mathematically done by deducting from its assets the liabilities of other undertakings. One will, therefore, have to give a reasonable interpretation to sub-rule(3) by adding after the words “borrowed moneys and debts due by the assessee”, the words “in respect of the industrial undertaking in which the capital employed is to be computed”. We accordingly hold that, on a true interpretation of rule 19A, in respect of each undertaking, the libilities of the assessee in respect of that industrial undertaking only are to be deducted from the aggregate value of the assets of the same industrial undertaking.

> The controlling words in sub-rule(1) viz., “for the purpose of section 80J the capital employed in an industrial undertaking....shall be computed....” must govern sub-rules (2) and (3).”

It is pointed out that the said judgment was also followed by the Gujarat High Court in C**ommissioner of Income Tax v. Cadila Chemicals P.Limited,** (2005) 278 ITR 633, wherein it was also noticed that the view of Bombay High Court has been accepted by the department.

In view of the above, this question has to be answered in favour of the assessee and against the revenue.

(Adarsh Kumar Goel)
Judge

Sept. 15, 2006 (Ajay Kumar Mittal)
'gs' Judge